

Minutes of the October 25, 2006 Meeting of the
Securities Industry Conference on Arbitration
PIABA Meeting, Tucson, Arizona

Deleted: New York Stock Exchange,
New York City

Members Participating in Person or by Phone

Amal Aly, SIA
Theodore Eppenstein, Public Member
Linda Fienberg, NASD
George Friedman, NASD
Greg Hoogasian, CBOE
Constantine Katsoris, Public Member and Chair
Karen Kupersmith, NYSE
Kenneth Meister, SIA
Pat Sadler, Public Member

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Invitees Participating in Person or by Phone

Joe Borg, NASAA
Karen Jalkut, AAA
Paula Jenson, SEC
Bryan Lantagne, NASAA
Gena Lai, SEC
Melanie Lubin, NASAA
Helene McGee, SEC
Elizabeth Sheridan, NFA
Tanya Solov, NASAA
Karen Tyler, NASAA

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Guests:

Phil Aidikoff, PIABA
Robert Banks, PIABA (outgoing president)
Scott Bernstein, PIABA
Steven Caruso, PIABA (incoming president)
Jenice Malecki, PIABA
Thomas Mason, PIABA
Jeff Sonn, PIABA
Mark Tepper, PIABA

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Deleted: Karen Tyler, NASAA 1

The Securities Industry Conference on Arbitration ("Conference" or "SICA") convened on October 25, 2006 at 8:30 a.m., Professor Constantine Katsoris, Chair, presiding.

ACTION ITEMS

Approval of Minutes of March 21, 2006 Meeting [Tab 1]

With minor amendments, the Conference approved the minutes unanimously. Mr. Sadler will finalize and distribute them.

It was noted that the SEC had received a Freedom of Information Act request from Les Greenberg (see item 3) for minutes of some past SICA meetings, and that the SEC had provided same.

Electronic Discovery [Tab 2]

SICA reviewed the work of the Electronic Discovery Subcommittee (Barbara Brady, Ms. Kupersmith, Mr. Meister, and Mr. Eppenstein). The group is also focusing on recent changes to the Federal Rules of Civil Procedure regarding electronic discovery, and will have an action item for the January meeting. It was reported that NASD is close to finalizing with the NAMC proposed changes to the Discovery Guidelines. Electronic discovery issues will be part of a second tranche. It was also reported that the American Arbitration Association (AAA) had developed training materials on electronic discovery, and that AAA might be able to provide them to the Conference. Mr. Hoogasian volunteered to join the subcommittee.

Petition for SEC Rulemaking [Tab 3]

During the summer of 2005 the SEC received two petitions for rulemaking, one from Les Greenberg and the other from Avery Goodman. In August, SEC's Catherine "Caitie" McGuire wrote to SICA Chairman Katsoris, asking that SICA consider the proposals. At the October 2005 SICA meeting, Chairman Katsoris appointed a subcommittee consisting of Mr. Eppenstein and Mr. Friedman (co-chairs), Jim Flynn (since replaced by Mr. Hoogasian), George Kramer, and Ms. Kupersmith to review the petitions. The subcommittee met several times over the past year, reporting periodically on progress.

SICA reviewed the subcommittee's work, and there appeared to be a consensus on the basic course of action. Because of the number of separate issues, the embedded action items were addressed seriatim with results indicated below.

I. Goodman proposal that claimants be permitted to appeal to an SEC Administrative Law Judge SRO decisions on removing arbitrators from a case, or arbitrator reclassification

The subcommittee did not favor creating for claimants (or respondents, for that matter) a broad right to appeal to an SEC Administrative Law Judge SRO decisions on arbitrator removal or classification, primarily because this would run counter to the goal of expedient administration of claims.

The subcommittee, however, recommended that SICA and SRO materials be amended to explain more carefully parties' rights for review of SRO administrative decisions in arbitration. Specifically, the subcommittee recommended that:

- The SICA *Guide to Arbitration*¹ (*Guide*) to be updated to state that, while SROs resolve most challenges to arbitrators by review of correspondence, a party can request that a conference call be convened with all counsel and the Director of Arbitration; and
- Directors of Arbitration should be encouraged to explain briefly the rationale for arbitrator removal/reaffirmation decisions, upon request. The SROs cautioned that

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¹ SICA's *Guide to Arbitration* is known formally as *Arbitration Procedures*.

providing such explanations should be discretionary with the Director, based on the unique facts and circumstances involved.

After some discussion, the following changes to the *Guide* were approved. Specifically, the section of the *Guide* titled "What are Challenges for Cause?" would read as follows (new language is underlined):

What are Challenges for Cause?

<No changes>

Opinion and Bias

<No changes>

Business or Personal Relationships

<No changes>

Previous or Current Involvement

<No changes>

Financial Interest

Arbitrator knows that she/he has, individually or as a fiduciary, or her/his spouse or minor child residing in her/his household has a financial interest in the subject matter in controversy or in a party to the arbitration proceeding, or any other interest that could be substantially affected by the outcome of the arbitration proceedings.

While most arbitrator challenges are resolved after the Director of Arbitration has reviewed the parties' relevant written submissions, a party can request that a conference call be convened with all counsel and the Director of Arbitration.

Each arbitrator must swear or affirm to render a fair and just award based on the documents and evidence presented by the parties. Also, unless the case is proceeding under an SRO rule that permits direct communication between the parties and arbitrators,ⁿ no party should attempt to communicate directly with any of the arbitrators. Such communication may render the decision of the arbitrator invalid. Any communication for the arbitrators must be addressed through the Director.

ⁿ See, e.g., SICA Uniform Code of Arbitration Rule 23(e).

Result: SICA concurred with the group's recommendations and approved unanimously these changes. NASD will handle making the changes to the *Guide*. There will also be further

discussion at SICA's January 2007 meeting on the issue of an "explained decision" from the Director of Arbitration on arbitrator removals/reaffirmations.

II. Greenberg proposal that arbitrators should be allowed to conduct independent legal research and that SROs should not restrict same

After some discussion over several meetings, the subcommittee coalesced around the following recommendations:

- *The Arbitrator's Manual* drafted by SICA should be updated to include in the appendix the revised 2004 *Code of Ethics for Arbitrators* (replacing the older version that was in the *Manual*);
- The *Manual* and perhaps the *Guide* should be changed to clarify when research would be permitted (for example, looking up cases cited in briefs); and
- The *Manual* and *Guide*) should be changed to refer to/include the inference in Canon VI(B) of the new *Code of Ethics* that some limited research is appropriate.

Each recommendation is addressed separately, below.

***The Arbitrator's Manual* should be updated to include in the appendix the revised 2004 Code of Ethics for Arbitrators (replacing the older version that was in the *Manual*):**

Result: This was completed in April 2006.

The *Manual* and the *Guide* should be changed to clarify when research would be permitted (for example, looking up cases cited in briefs): The subcommittee recommended that the section of *The Arbitrator's Manual* entitled "Before the Hearing" be amended to address this issue. After some discussion at the SICA meeting, the following changes were proposed (new language is underlined; deleted language is in strikethrough

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(The preceding portion of this section is unchanged.)

Arbitrators should not make independent factual investigations. The arbitration case belongs to the parties, and the parties should present the facts as they wish. Nothing, however, prohibits an arbitrator from reading the text of a rule, statute, or legal citation referred to in a party's pleading (e.g., if the complaint charges a violation of a suitability rule, the arbitrator may read the rule). ~~If an arbitrator believes that the pleadings require clarification or that a pleading or document is missing, he or she should call the staff immediately. A request for clarification at this juncture is preferred so the initial hearing is not wasted.~~

When in doubt about an issue, legal or otherwise, arbitrators should request briefs from the parties. If cases are cited in a party's motion or brief, and the arbitrators wish to read the full court opinions, the arbitrators should ask the parties to supply copies, and if necessary, the arbitrators may look up the cited authorities themselves. Arbitrators generally should review only those materials presented by the parties to the arbitrator.

In those limited instances where an arbitrator believes that independent research is appropriate, as described above, the arbitrator should disclose the nature of that research to the parties. By doing so, the arbitrator makes the parties aware of the matters being considered by the arbitrator and the parties may respond accordingly.

The Code of Ethics requires that arbitrators keep confidential all matters relating to the arbitration proceedings and decision. However, the Code of Ethics also states that "an arbitrator may obtain help from an associate, a research assistant or other persons in connection with reaching his or her decision if the arbitrator informs the parties of the use of such assistance and such persons agree to be bound by the provisions of this Canon."

(The remaining portion of this section is unchanged.)

Results:

1) SICA concurred with the subcommittee's recommendations and approved these changes by a vote of 6-Yes, 0-No, and 1-Abstention. NASD will handle making the changes to the *Manual*.

2) Also, since there is no analogous section in the *Guide*, the subcommittee recommended and SICA approved by the same vote placing the identical language set forth above into the *Guide*, in the "What if I Don't Get Paid?" section of the *Guide* (where the arbitrators' decision-making authority is discussed). NASD will handle making the changes to the *Guide*.

3) Last, the subcommittee noted that it had been six years since *The Arbitrator's Manual* and the *Guide* have had a comprehensive review and update. In light of developments over the past six years, the subcommittee recommended that SICA commence such a review. The chair appointed a subcommittee consisting of Ms. Aly, Mr. Friedman, Mr. Hoogasian, Ms. Kupersmith (Chair), and Mr. Sadler to undertake this effort. Ms. Brady and Rick Berry of NASD may substitute for Mr. Friedman, and Mr. Meister may substitute for Ms. Aly.

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The *Manual* and *Guide* be changed to refer to include the inference in Canon VI(B) of the new *Code of Ethics* that some limited research is appropriate.

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Result: This is accomplished with the changes discussed above.

III. Greenberg proposal that SROs with arbitration programs conduct party evaluations and peer evaluations (on a mandatory basis)

The SROs all reported that they have existing, voluntary party and peer evaluation programs. At its January 2006 meeting SICA agreed that, while parties and arbitrators should be encouraged to complete survey forms, a mandatory program was not necessary or appropriate. SICA directed the subcommittee to further consider ways of improving the response rate.

The subcommittee recommended the following measures to promote a better response rate for peer and party evaluations:

- **Putting surveys online:** allowing responders the option of completing surveys online should increase response rates. The Web has become an accepted tool for completing surveys, and offering this additional means of responding is a good idea. NASD already offers this option for both the party and peer evaluations;
- **Including return postage:** providing return postage will encourage some responders to complete and return the survey form. Some SROs, such as NYSE and NASD, already do this.
- **Reminding arbitrators about peer reviews when they get paid:** this would appear to be a good time to remind arbitrators to complete peer reviews.
- **Encouraging settling parties to return surveys:** some SROs limit user surveys to cases in which arbitrators issue awards. However, there is value in also asking parties who settle their case to complete and return surveys, since in many of those cases, arbitrators will have been appointed and may have held initial or evidentiary hearings. If arbitrators have not been appointed, or have not acted, the responding parties will simply check off the "not applicable" option.

Result: SICA concurred with the group's recommendations and approved unanimously these recommendations to the SROs.

SICA then reviewed additional proposals in the petitions where the subcommittee believed action was not warranted. These are discussed below:

IV. Greenberg proposal to eliminate the industry arbitrator or that, in the alternative, the industry arbitrator be required to disclose to the parties any information he or she presents to the other arbitrators in deliberations

The subcommittee deferred consideration of these issues to SICA's broader efforts at reviewing arbitrator classification. There was a discussion at the SICA meeting about the second part of the recommendation, i.e., to what extent should deliberations be disclosed.

Result: There emerged a consensus that this was not a good idea, and if implemented would compromise arbitrator independence. However, the group undertaking the comprehensive review of the *Guide* and *Manual* will consider this general topic.

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V. Greenberg proposal that SROs be required to train arbitrators in applicable substantive law

The subcommittee recommended that this proposal not be adopted, because: 1) it would not be feasible or appropriate to train arbitrators on the law of 50 states; 2) keeping abreast of changes in substantive law would be very difficult; 3) it would likely be very difficult to obtain a consensus on the content of such training; 4) it is generally up to the parties to bring their case to the arbitrator (including addressing substantive law); and 5) strict application of the law could in many instances be harmful to investors.

Result: SICA concurred with the group's recommendations.

VI. Greenberg proposal that SROs include in their predispute arbitration agreements whether their arbitrators are trained in the law and required to follow it. Also, they should be required to disclose their arbitrator evaluation process

For the reasons articulated above, the subcommittee recommended that the first part of this proposal should not be adopted. The second part is moot, since the SROs *do* disclose the nature of their arbitrator evaluation processes.

Result: SICA concurred with the group's recommendations.

VII. Greenberg proposal that SEC specifically oversee whether SROs are following the first 5 proposals

The subcommittee believed this is self-evident and somewhat premature (since the proposals have not been approved). SEC already oversees SRO conduct under approved rules.

Result: SICA concurred with the group's recommendations.

VIII. Recent Correspondence from Mr. Greenberg

Chairman Katsoris reported that, in August and September, he had received several letters from Mr. Greenberg, among other things inquiring about: 1) the status of SICA's review of his petition; 2) whether he would be getting a copy of SICA's report on his petition; and 3) SICA's membership and governance. Mr. Greenberg also expressed his opinion that SICA was a "Federal Advisory Committee" and that, because it was not operating in conformity with the federal legislation governing such committees, it was inappropriate for SICA to advise the SEC on his petition. Ms. McGuire and certain members of SICA were copied at various times on this correspondence. Chairman Katsoris had a email dialogue with Mr. Greenberg in which he: 1) advised Mr. Greenberg of the status of SICA's review; 2) advised Mr. Greenberg that SICA would not be furnishing him a copy of any "report" or other results, because this information was not public and would eventually be provided by SICA to SEC; 3) provided general background

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and governance information on SICA; and 4) did not take a position on whether SICA was a Federal Advisory Committee. Some members noted that the SEC does not compensate SICA members and the SEC does not set the agenda for SICA meetings or actions.

Result: No action was taken.

Chairman Katsoris stated that he would write to Ms. McGuire, to advise her of the outcome of SICA's consideration of the issues raised in the petitions.

Digital Recording of Hearings [Tab 4]

SICA considered a proposal recommending that the SICA Uniform Code of Arbitration (Section 25(d)) with the recently approved change to NASD's Code of Arbitration Procedure, authorizing digital or other recording in addition to analog tape recording of hearings.

Result: The motion was approved unanimously. Ms. Kupersmith will revise the Uniform Code.

Conforming SICA's Eligibility Rule with *Howsam* [Tab 5]

It was proposed that Section 12 of the Uniform Code be amended to conform to the Supreme Court's holding in *Howsam v. Dean Witter Reynolds, Inc.* Similar to the already-approved and implemented change to NASD's Code of Arbitration Procedure, this change would provide that arbitrators, and not the SRO fora, decide eligibility issues.

Result: A consensus emerged to pursue this change. Ms. Kupersmith will prepare an Action Item for the January 2007 meeting.

DISCUSSION ITEMS

SICA Governance [Tab 6]:

At the June 13th SICA meeting, Chairman Katsoris noted that public member Mr. Eppenstein's second term is expiring at the end of this year, and that it would be a good time to look at SICA governance issues. Toward that end, he asked Mr. Friedman to chair an informal task group to "tee up" the issues of term limits for public members and voting rights for SROs, to be discussed at the October SICA meeting. The other members of the group are: Lourdes Gonzalez (or another representative from SEC), Mr. Hoogasian, Ms. Kupersmith, Mr. Mennes, Mr. Meister, and Mr. Sadler. The group met by teleconference on July 11th, attended by Messrs. Friedman, Hoogasian, Meister, and Sadler, and SEC staff members Ms. McGuire, Ms. Jenson, and Ms. Lai. It addressed separately the two core topics: term limits for public members and SRO voting rights.

Results:

- 1) After a brief discussion, it was determined that between now and the January meeting, the public members would meet and discuss the issue of Mr. Eppenstein's replacement. In the interim, as provided in SICA's governance, Mr. Eppenstein will continue to serve

until he is replaced, and he will attend the January 2007 meeting. The remaining issues were tabled until the January meeting.

- 2) It was suggested that the SICA Roster indicate voting and non-voting members. NASD will handle this change.

Independent Research on the Fairness of SRO Arbitration [Tab 7]:

It was reported that the contract was signed, and was being sent to Pace University. The survey is finalized, and his subcommittee will review the newly-formatted document, approve it, and launch the survey.

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Result: Mr. Sadler will report on the survey's status at the next meeting.

Arbitration of Employment Disputes [Tab 8]:

Mr. Eppenstein asked the SROs for a progress report on his proposal that they take some action to counteract recent court decisions that appear to allow a firm to preclude an employee from exercising his or her right to arbitrate at an SRO forum. At the January meeting, SICA adopted a resolution urging the SROs to issue a Notice to Members precluding this practice (similar to NASD Rule 3110(f) for customer disputes), and that SROs adopt rules similar to SICA Uniform Code of Arbitration Rule 1, allowing an employee to require arbitration at an SRO irrespective of whether there is an arbitration agreement (i.e., a rule similar to NASD Rule 10301 for customers).

Result: No action was taken.

Bonding Requirements for Unpaid Awards [Tab 9]:

At the June meeting, it was noted that there is a proposed National Futures Association (NFA) rule that requires a party moving to vacate an arbitration award to post a bond. Chairman Katsoris recalled that SICA had looked at this issue in the past, but agreed to appoint a subcommittee to examine this issue consisting of Mr. Sadler, Mr. Meister (co-chairs), and Kenneth Andrichik. Liz Sheridan of NFA will be present to report on the new rule.

Result: Tabled until the January 2007 meeting.

Arbitrator Disqualification Criteria [Tab 10]:

At the June meeting, the chair appointed a subcommittee to review the SICA temporary and permanent removal criteria, and recommend action at the October or January meetings. The subcommittee is: Ms. Feeney (Chair), Mr. Eppenstein, Mr. Meister, Ms. Kupersmith, and Ms. Brady. The group will present its results at the January 2007 meeting.

Result: Subcommittee to propose action for the January 2007 meeting.

Additionally, Mr. Eppenstein asked that SICA discuss at the next meeting the following two related issues: 1) consequences when arbitrators refuse to answer *voir dire* questions; and 2) consequences for material misstatements or omissions in arbitrator disclosures.

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Result: Mr. Eppenstein will prepare a discussion item for the January 2007 meeting.

Arbitrator Rights [Tab 11]: Tabled until the January meeting.

Litigation Abuses in Arbitration [Tab 12]: Tabled until the January 2007 meeting.

INFORMATION ITEMS

Update/Statistics on NASD Pilot Procedures for Elderly, Infirm, and Terminally Ill Parties [Tab 13]

It was reported that anecdotal evidence indicates that NASD's pilot program has been effective in expediting hearings for elderly, infirm and terminally ill parties. NASD is planning to evaluate the results in the beginning of 2007. NASD will report again at the January meeting.

Update/Statistics on Direct Communication Rule [Tab 14]

It was reported that anecdotal evidence suggests the rule has been well received. NASD is considering doing a survey next year to gauge constituent views of the new rule. No action was taken. NASD will report again at the January meeting.

SRO Reports on Activities and Rule Filings [Tab 15]

The SRO representatives present updated the Conference on recent activities and rule filings.

Schedule of Future Meetings [Tab 16]

The Conference reviewed the scheduled 2007 SICA meetings. Chairman Katsoris noted that the planned January 17 meeting date conflicted with his teaching schedule, and asked that the date be changed to January 16th. SICA agreed to change the date. Also, Mr. Kramer has rotated off as SIA representative, and has been replaced on an interim basis by Amal Aly. As revised, the meeting schedule is as follows (host's name in parenthesis):

- January 16 in New York City at NASD (George Friedman) ***10 a.m. start time
- March 27 in Phoenix at SIFMA Compliance and Legal Division Annual Meeting (Amal Aly) *** 1 p.m. start time
- June 14 in New York at NYSE (Karen Kupersmith)
- October 17 in Amelia Island, Florida at PIABA's Annual Meeting (Pat Sadler)

Cases and Articles of Interest [Tab 17]:

No discussion.

MEETING WITH PIABA DELEGATION

The Conference was joined for lunch by a PIABA delegation consisting of Phil Aidikoff, Robert Banks (outgoing president), Scott Bernstein, Steven Caruso (incoming president), Jenice

Malecki, Thomas Mason, Jeff Sonn, and Mark Tepper. Steve Caruso outlined the following items of importance to PIABA:

- Mandatory Use of an Industry Arbitrator in Investor Cases: PIABA's leadership believes mandatory use of the industry arbitrator in investor cases should be eliminated.
- "Conflicted" Public Arbitrators: PIABA believes that public arbitrators should not have significant ties to the industry.
- Delays in SEC Rule Approval Process: PIABA is concerned with how long it takes SEC to review arbitration-related rule filings.
- Dispositive Motions: PIABA's members report a significant increase in the frequency of dispositive motions.
- Arbitrator Disclosure Reports: PIABA believes there should be a "zero tolerance" policy for material misstatements or omissions in arbitrator disclosure reports
- Pro Se Parties: PIABA is concerned about the growing complexity of the arbitration process.

The PIABA delegation departed at 1:00 p.m.

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ADJOURNMENT: meeting adjourned at 2:00 p.m.